

## Article Information

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Service: Property & Development

Sector: Real Estate

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## Land Tax Amendments - Are you prepared?

**The South Australian Government has defiantly issued its Land Tax (Miscellaneous) Amendment Bill 2019 (Bill) for consultation manifesting a clear intent on the part of the Government to shut what some members of the Government have labelled “loopholes”, alter the way land tax is aggregated and introduce new bases for taxing certain types of trusts.**

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### Current Status

The South Australian Government has defiantly issued its Land Tax (Miscellaneous) Amendment Bill 2019 (**Bill**) for consultation manifesting a clear intent on the part of the Government to shut what some members of the Government have labelled “loopholes”, alter the way land tax is aggregated and introduce new bases for taxing certain types of trusts.

The timing of the Bill has been criticised by property, construction, business and investment groups on the basis that it coincides with the implementation of a State wide revaluation which seemingly will result in marked increases to site values culminating in a significant revenue grab in favour of the Government.

To put this in context, Colliers International has recently undertaken analysis of the impact of the revaluation and has advised that early reports from the first stage of the revaluation process (which came into effect on 1 July 2019), and included the local government assessments of Unley, Walkerville and the Adelaide Plains, indicates site values have increased by up to 40%. This demonstrates that the Valuer General’s assessments of site values are likely to markedly increase from historically conservative levels.

The Adelaide CBD is scheduled for the next round of reviews with newly assessed site and capital values to be released for use in the 2020/21 financial year.

The revaluation overlayed with a tightening to aggregation is likely to result in significant increases in land tax for many owners with multiple holdings. Many stakeholders believe this will spark a property sell off and discourage investment in the State, damaging an industry which is the driving force behind our economy.

Treasurer Lucas has indicated that the total tax to be derived from the new measures will rise to \$86M, up from his \$40M estimate made in June. The material discrepancies in forecast revenue, lack of consultation and limited financial and economic analysis by the Government since the release of its budget have been the subject of much criticism. The Treasurer has announced in Parliament that the Government will not negotiate on changes to aggregation and that *“[t]he nature of the consultation will be in relation to the technical detail of the drafting of the bill”* ruling out any scope for wholesale changes to be made to the Bill.

Policy pundits remain hard at work with the Property Council of Australia, Business SA and Urban Development Institute of South Australia continuing their strong efforts to fight for the complete abolition of the aggregation proposal. They argue that the reform when coupled with the comprehensive revaluation process is damaging confidence in the property sector as evidenced by the Business SA / William Buck June quarter survey of business expectations which revealed a confidence fall to 84.4 points (down from 116.4 in December).

In view of the Government’s hard line, it is imperative that property owners understand the proposed amendments and implement the most effective ownership structure(s).

## Amendments to the Land Tax Act 1936 (SA) (“the Act”)

The amendments to the Act are proposed to come into force from 1 July 2020.

### Rates

The top land tax rate has been reduced to 2.4% (which is still higher than VIC and NSW but lower than WA and QLD). The Government has also indicated that the tax free threshold will increase to \$450,000. The proposed rate structure with respect to trust and non-trust structures is as set out below:

#### 2020-21 estimated scales (non-trust)\* (herein referred to as general land tax rates)

\$0	to	\$450,000	0	+	0.00%
\$450,001	to	\$755,000	0	+	0.50%
\$755,001	to	\$1,098,000	\$1,525.00	+	1.65%
\$1,098,001	&	over	\$7,184.50	+	2.40%

#### 2020-21 estimated scales (trust)\* (herein referred to as surcharge rates of land tax)

\$0	to	\$25,000	\$0	+	0.00%
\$25,000	to	\$450,000	\$125.00	+	0.50%
\$450,001	to	\$755,000	\$2,250.00	+	1.00%
\$755,001	to	\$1,098,000	\$5,300.00	+	2.15%
\$1,098,001	&	over	\$12,674.50	+	2.40%

\*Thresholds are indexed annually and subject to change.

For comparative purposes, the current scales are as follows:

#### 2019-20 scales

\$0	to	\$391,000	\$0	+0.00%
\$391,000	to	\$716,000	\$125.0	+0.50%
\$716,000	to	\$1,042,000	\$1,625.0	+1.65%
\$1,042,001	to	\$1,302,000	\$7,004.0	+2.40%
\$1,302,000	and over		\$13,244.00	+3.70%

### Aggregation

There are provisions in the Bill which are designed to group “related corporations”. Companies will be related where a person or group of persons (with the term “person” to include a company):

- controls the composition of the board of directors of each company;
- is able to cast, or to control the casting of, more than 50 per cent of the maximum number of votes that might be cast at a general meeting of each company; or
- holds greater than 50 per cent of the issued share capital of each company.

The aggregation principles also aggregate an owner’s partial or indirect interest in land, rather than only aggregating properties held in a group ownership structure. The land tax assessment will be calculated on an investor’s indirect or partial interest in the land as well as land wholly owned by the investor.

### Unit Trusts

With respect to land owned by unit trusts, the Bill provides that:

- the trustee will be subject to surcharge rates of land tax (refer to proposed rate structure above) unless the trustee of the unit trust lodges a written notice of the unitholding scheme with the Commissioner for State Taxation (**Commissioner**);
- the trust surcharge rates are higher than general land tax rates and apply if the total value of the taxable land held by the trust is more than \$25,000;
- where the Commissioner is notified of the unitholders in the unitholding scheme:
  - each unit holder will be deemed for the purposes of the Act to be the owner (but not to the exclusion of the

trustee) and will be assessed proportionately to their beneficial interest in the subject land together with any other taxable land owned by the unitholder;

- the trustee will also be liable for land tax at the general rates as if the land was the only land owned by the trustee; and
- to avoid double taxation, the land tax payable by the unitholder will be subject to a deduction to its land tax liability according to a formula which has regard to the land tax paid by the trustee. If the deduction will result in a negative amount payable, the unitholder will not receive any credit to any land tax it is liable to pay under the Act.

## **Discretionary Trusts**

Discretionary trusts will not be aggregated. However, land held by trustees of discretionary trusts will be subject to surcharge rates of land tax unless the trustee provides written notice to the Commissioner nominating a designated beneficiary as the owner of existing land held in the trust for the purposes of the Act. Only one beneficiary may be nominated and he/she must be a natural person above the age of 18 on the “prescribed day” (being the day on which the draft legislation is introduced to the House of Assembly). Nomination does not result in the nominated beneficiary having any interest in or entitlements in respect of the property different from those enjoyed prior to the nomination.

The nomination must be accompanied by a statutory declaration from the nominated beneficiary and must be made no later than 30 June 2020. Where a nomination is made:

- the trust will not be subject to surcharge rates in respect of “pre-existing trust land” (being land held by the relevant discretionary trust on the day on which the draft legislation is introduced to the House of Assembly);
- the beneficiary will be deemed for the purposes of the Act to be the owner (but not to the exclusion of the trustee) and will be assessed proportionate to the designated beneficiary’s beneficial interest in the subject land together with any other taxable land owned by the beneficiary; and
- to avoid double taxation, the land tax payable by the beneficiary will be subject to a deduction to his/her land tax liability according to a formula which has regard to the land tax paid by the trustee. If the deduction will result in a negative amount payable, the beneficiary will not receive any credit to any land tax he or she is liable to pay under the Act.

However, any “subsequent trust land” (being land acquired by the relevant discretionary trust after the day on which the draft legislation is introduced to the House of Assembly) held by the discretionary trust will be subject to surcharge rates.

Superannuation trusts and other specific trusts (including charitable trusts and deceased estates) will not be required to pay the trust surcharges and are excluded from the new regime.

## **Prudent Planning**

Taxpayers will also need to address the following:

- Identify the trusts within the relevant group and determine whether the trusts fall within the category of discretionary trust, unit trust or fixed trust.
- Consider how the controlling interest provisions will apply to companies within a large group where the shares in the companies are owned by discretionary trusts with different trustees. There may be different controlling interests (and not necessarily an identical overlap in control) which should be considered within the group structure.
- Notification and disclosure requirements will need to be complied with by taxpayers including (in addition to the notification requirements specified above):
  - all trustees of land in SA must notify the Commissioner within one month after acquiring or disposing of land in SA;
  - trustees owning existing land must notify the Commissioner of their existing land holdings within month after the commencement of the amendments implemented by the Bill; and
  - trustees of unit trusts will be required to notify the Commissioner of any change to the unitholdings in the scheme within one month after such change.
- With respect to unit trusts, the directors of the trustee should consult with unitholders to assess whether it would be in the unitholders’ best interests to notify the Commissioner of the unitholdings in the unit trust scheme to circumvent the payment by the trustee of the trust surcharge. A cost benefit analysis should be undertaken with respect to the potential land tax saving for the trust as against the financial burden or cost to each unitholder where it is deemed to be the “owner” for the purposes of the Act.
- With respect to trustees of discretionary trusts, the trustee should undertake an analysis as to whether a beneficiary should be nominated and who that beneficiary should be having regard to other interests in land that

are held by that beneficiary or which may be acquired in the future.

- The shareholder and director composition of companies within a group should be considered to determine whether a controlling interest arises by virtue of the shareholding structure or board control (including arrangements influencing voting rights at the director level).
- There may be restructuring opportunities available for larger groups. However, the anti-avoidance provisions must be considered in the process of any restructure.

A trustee of a fixed trust or unit trust which lodges a notice identifying the beneficial interests in land and subsequently withdraws such notice will be precluded from lodging another notice with the Commissioner in relation to the trust. Upon the withdrawal of the notice, the relevant trust will forfeit the right to have the general land tax rates apply to the relevant trust. On that basis, the decision to issue and/or withdraw a notification should be the subject of rigorous analysis and diligent decision making.

### **Example**

The proposed reforms will in most cases be detrimental to investors with multiple land holdings. To put this into perspective, we have used the example of Trevor and applied the background facts to various ownership structures.

#### Background Facts

Trevor is a sole trader plumber who has saved hard over the course of his work life. Trevor has managed to put together a modest residential property portfolio here in SA made up of six properties. The land value of each property is \$500,000. At the moment he pays \$545 land tax on each property as he has used different forms of ownership for each property and therefore is not aggregated - this gives rise to a total land tax liability of **\$3,270** for this financial year.

#### Company Structure

If Trevor owns the 6 properties in companies which are controlled by Trevor, Trevor will be subject to the principles of aggregation and consequently his companies will be required to pay a total of **\$52,832.47** under the new regime.

#### Discretionary Trusts – No Designated Beneficiaries

Trevor is likely to have acquired his properties in discretionary trusts which until now has been a prudent structuring method for land tax purposes and from a CGT perspective. Applying the new surcharge rates of land tax, each trust will have a land tax liability of \$2,749.99 with a total land tax liability of **\$16,500** (assuming there is no nomination of a designated beneficiary).

#### Discretionary Trusts – Designated Beneficiaries

If Trevor nominates a separate individual beneficiary to each trust, these individual beneficiaries will be deemed for the purposes of the Act to be the owner (but not to the exclusion of the trustee). Each trust will be taxed at general land tax rates giving rise to a land tax assessment of only **\$250** on each property (a total of \$1,500). This amount will be deducted from the land tax payable by each designated beneficiary. Assuming the six designated beneficiaries do not own any other properties in SA (or own properties which are exempt from land tax under the Act such as a principal place of residence or agricultural investment), each designated beneficiary will not be required to pay any further land tax.

If any of the designated beneficiaries hold other land holdings which are not exempt under the Act, those holdings will be aggregated together with any other taxable land owned by the designated beneficiary (with any land tax payable by the relevant trustee to be deducted from land tax payable by the designated beneficiary).

The above examples illustrate the benefit in nominating beneficiaries in the case of discretionary trusts to reduce land tax. However, it is clear that Trevor will be worse off if he receives an assessment based on surcharge rates of land tax or has a group of related companies owning the properties.

### **Concluding Remarks**

Although the Government has finally relented to pressure and reduced the top rate from 3.7% to 2.4% from 1 July 2020, the top rate kicks in at a threshold generally much earlier (i.e. lower) than other States. The Bill still presents a heavy burden for the investment community and a dampener to business and investment confidence in the State.

In the authors' view, the Government should not embark on such drastic reforms until the impact of the revaluation initiative is fully understood. This is reckless policy in view of the uncertainty surrounding the revaluation initiative and likely escalating site values arising from this process.

The land tax rates particularly in view of the relatively low thresholds, remain very uncompetitive when compared to other States and given the higher reliance in South Australia on net income returns on properties (as distinct from the significant capital growth which occurs in the eastern States) is a major anti-investment tax that will drive investment away from South Australia.

It is a complex, somewhat arbitrary tax that not only is at high rates, but attacks and discriminates against people who choose South Australian real estate as their main basis for establishing retirement income. Many people will be better off limiting their South Australian real estate portfolios considerably and looking to invest either in non-real estate assets or, more likely given many individuals' reluctance to invest in the stock market, they will take their investment money out of South Australia and place it in other States.

We would prefer to see:

- a simpler regime with a lower, flat rate of land tax applied broadly irrespective of the nature of ownership;
- the removal or reduction of exemptions; and
- if different rates are to be maintained, then competitive rates and thresholds so as to attract investment into SA.

Piper Alderman is maintaining a close watch on the status of the Bill and will be actively involved during the consultation period relating to the Bill. We will be able to assist in advising on the impact of the amendments to the Act as they apply to current circumstances and we will also be able to assist with compliance issues.